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TREASURY FOR L LAMONICA

E.O. 12958: NA
TAGS: ECON EFIN JM
SUBJECT: JAMAICA OVERHAULS PENSION SYSTEM

¶1. Summary: The Senate has approved the contentious Pensions (Superannuation Funds and Retirement Schemes) Act to reform and regulate the pensions industry in Jamaica. The Act was passed in 2004 and came into effect on March 1, 2005, but the regulations supporting the Act were sent to a Senate Committee for review amid concerns that some of the regulations were onerous. A number of stakeholders in the pensions industry remain concerned about the high costs associated with regulation and the amount of power vested in the hands of the regulator, the Financial Services Commission (FSC). The GOJ is also disturbed about the lack of consensus on vesting and portability of pension rights and has signaled its intention to pursue these issues in a second phase of reforms. Despite these concerns, this should bring order and security to retirement savings, while providing a substantial pool of funds for long-term investment. End summary.

Background

¶2. Nearly two years after its passage in the Lower House of Parliament, on March 19 the Jamaican Senate finally approved the controversial Pensions (Superannuation Funds and Retirement Schemes) Act, 2004, paving the way for the Financial Services Commission (FSC) to become the regulator of pension funds and schemes in Jamaica. The process to develop pensions legislation for the private sector commenced almost ten years ago, but was largely stymied by resistance from trade unions and some industry players.

¶3. Prior to the passage of the act, pension legislation was mainly found in the Income Tax Act of 1954, although the Income Tax DepartQnt did not have the legal authority to supervise the industry. The Act is therefore an attempt by the GOJ to reform the pension system, ensuring that a proper legislative and regulatory framework is instituted to secure the interests of pensioners in the over 1,500 registered pension schemes in Jamaica. This is particularly important given the meltdown of the financial sector in the 1990s which reflected, inter alia, the imprudent management of the country's pension funds.

¶4. Under the new act, all approved pension funds and schemes must be registered with the FSC. Likewise, all

managers and administrators of pension funds must be licensed and all trustees must be registered. The regulator will also have the power to monitor the operations of the industry as well as demand the disclosure of information to the agency and fund members. Additionally, the legislation includes investment limits, and allows self-employed persons and persons in non-pensionable jobs to save for retirement.

Dissent

¶5. Trade unions are opposed to the issues of vesting and portability, contending that persons should have the option to reclaim their contribution refunds, should they so desire. Currently, persons can opt for a refund of their mandatory contributions in the event that they leave their employment for another opportunity. It concerns the GOJ, however, that - once obtained - these "refunds" are generally used for consumption purposes, leaving many retirees without sufficient resources for retirement.

¶6. Industry players, on the other hand, dislike the supporting regulations to the Act due to: (1) the costs associated with bringing the industry in line with the requirements of the act and regulations; (2) the perceived burden of compliance; and, (3) legal questions surrounding offences and penalties, particularly the subjection of trustees to criminal prosecution. It was these concerns that prompted the Senate to send the act and regulations to a select committee for review.

¶7. Patrick Lynch, Chairman of the Gordon "Butch" Stewart group of companies pension scheme, one of the largest in the country, has estimated that pensioners will lose some

USD 2.3 million of the approximately USD 2.3 billion under management annually. Lynch has also reiterated his strong objection to the FSC being given control over private pension funds and retirement schemes, including the authority to refuse the dissolution of a fund or scheme even if the trustees agreed to do so.

¶8. William McConnell of the Lascelles DeMercado Group (and prominent member of the Private Sector Organization of Jamaica) argued that regulatory fees amount to a new "tax" on retirees. Some detractors also argue that the regulations impose costs that could wipe out a number of the smaller pension schemes. However, Minister of Finance Omar Davies and Executive Director of the FSC Brian Wynter have countered by suggesting that the policy of levying charges to cover the cost of regulation is universally accepted. Davies said the GOJ'S sole interest in the matter is the protection of the savings of contributors and the treasury would not benefit from the passage of the legislation.

GOJ Concerns Left Unaddressed

¶9. Despite trade union pressure, the GOJ wished to include vesting and portability of pension rights as part of the reformed pension landscape. These rights are expected to ensure that persons are more prepared for retirement and would prevent them from claiming any refund of their contributions before retirement. While GOJ officials and other industry players agreed that vesting and portability rights were necessary, trade unions insisted that persons should be allowed to claim for refunds. With the deadlock stalling the reform process, the GOJ eventually decided to postpone the issue, but signaled its desire to pursue the issue in a second phase of reforms. In fact, Davies has announced his intention to establish a task force comprising representatives of the various stakeholders as well as FSC officials to consider this and other measures.

Comment

¶10. The approval of the Pensions Act will add an important layer of regulation to the financial sector, bringing the country's regulatory framework closer to international standards. This is particularly important given that the imprudent management of pension funds was one of the underlying reasons for the mid-1990s financial sector crisis. The improved regulations intend to provide greater protection for retirement savings in a country with a limited social safety net. The reform process is therefore likely to bring some order to the way that pension funds of approximately USD 2.3 billion are invested. It also provides a significant pool of long-term savings, given Jamaica's relatively young population, for investment in long-term projects. Already, pension funds are looking forward to the possibility of investing in infrastructural projects like toll roads, which are turning out to be relatively lucrative investments. Nevertheless, real concerns remain, chief among them the costs associated with meeting the regulations and the impact of the new regulations on small funds.

¶11. Comment (cont'd): While the cost of regulation is not a tax on the industry, it could hurt some funds, especially in a low interest rate, high inflation environment. Small funds could find it difficult to comply with some of the regulations and might be forced to dissolve. The issues of vesting and the portability of pensions (to ensure that persons are more adequately prepared for retirement) cannot be overstated, and one can expect a second phase of reform by the GOJ to be imminent. End comment.

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